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No. 680

IN THE

Supreme Court of the United States

OCTOBER TERM, 1970

CONTINENTAL OIL COMPANY, ET AL.,
Petitioners,

v.

FEDERAL POWER COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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September 14, 1970

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INDEX

	Page
Opinions Below	1
Jurisdiction	2
Questions Presented	2
Statutes Involved	4
Statement	4
Reasons for Granting the Writ	15
Conclusion	26
Appendices	Under separate cover

CITATIONS

CASES:

Baltimore & Ohio R. Co. v. *Aberdeen & Rockfish R. Co.*, 393 U.S. 87 (1968) 3, 21

Bluefield Water Works & Improvement Co. v. *Public Service Commission*, 262 U.S. 679 (1923) 21

Civil Aeronautics Board v. *Delta Air Lines*, 367 U.S. 316 (1961) 19

D. C. Transit System Inc. v. *Washington Metropolitan Area Transit Commission*, 350 F.2d 928 (D.C. Cir. 1965) 3

Federal Power Commission v. *Hope Natural Gas Company*, 320 U.S. 591 (1944) 3, 21

Federal Power Commission v. *Idaho Power Co.*, 344 U.S. 17 (1952) 17

Federal Power Commission v. *United Gas Pipe Line Co.*, 393 U.S. 71 (1968) 17

International Union v. *Eagle-Picher Mining & Smelting Co.*, 325 U.S. 335 (1945) 19

Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 2, 5, 10-11, 12, 16, 17, 18-19, 20-23, 24, 25

Securities and Exchange Commission v. *Chenery Corp.*, 318 U.S. 80 (1943); 332 U.S. 194 (1947) 17

	Page
Sunray Midcontinent Oil Co. v. *Federal Power Commission*, 353 U.S. 944 (1957)	16, 17, 18
Tacoma v. *Taxpayers of Tacoma*, 357 U.S. 320 (1958)	19
United States v. *Seatrain Lines, Inc.*, 329 U.S. 424 (1951)	19
Wisconsin v. *Federal Power Commission*, 373 U.S. 291 (1963)	24
STATUTES:	
Judicial Code, 28 U.S.C., Section 1254(1)	2
Natural Gas Act,	
Section 4(a), 15 U.S.C. 717c(a)	4
Section 4(e), 15 U.S.C. 717c(e)	4, 9
Section 5(a), 15 U.S.C. 717d(a)	4
Section 16, 15 U.S.C. 717o	4, 13
Section 19(b), 15 U.S.C. 717r(b)	2, 3, 4, 6, 12, 14, 16, 17, 18, 19

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Continental Oil Company, *et al.* (Continental, *et al.*), petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in this case on March 19, 1970.

OPINIONS BELOW

The opinion of the Court of Appeals (Appendix A, pp. 1-70) and its opinion on petitions for rehearing (Appendix, B, pp. 1-3) are not yet reported. The opinions and orders of the Federal Power Commission (Appendices D, pp. 1-256, and E, pp. 1-112) are reported at 40 FPC 530 and 41 FPC 301. The opinion of the Hearing Examiner (III J. A. (I) 62d-447d) is reported at 40 FPC 703.[1]

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[1] Under separate cover, Continental, *et al.*, are filing the Appendices to this Petition. Continental, *et al.*, are also filing the

JURISDICTION

The judgment of the Court of Appeals was entered on March 19, 1970 (Appendix C, p. 1) and was clarified by an opinion and order denying petitions for rehearing entered on June 16, 1970 (Appendix B, pp. 1-3). We invoke the jurisdiction of this Court under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTIONS PRESENTED

1. Whether the Court of Appeals erred in refusing to enter an order reversing and remanding the case to the Federal Power Commission after: (a) the Commission, in response to inquiry from the Court of Appeals, formally requested a remand; (b) the Court of Appeals expressed its view that the opinions and orders on review were deficient and Commission reconsideration was warranted; (c) the Court of Appeals had found the Commission's opinion and orders inadequate and incomplete, particularly as to findings on critical issues of a national and area natural gas supply deficiency and of industry capital requirements for exploration and development; and (d) the record showed; and the Court of Appeals recognized, that the Commission had misinterpreted and failed to apply this Court's decision in the *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).

2. Whether the Commission unlawfully ordered rate reductions and refunds by failing to follow *Permian* and failing to make required findings upon: (a) demand for natural gas and the supply needed to meet that demand:

Joint Appendix in the Court of Appeals which consisted of four volumes designated as Part I and two volumes designated as Part II. The citation "III J. A. (I) 62d" therefore refers to Volume III of Part I, page 62d. Such page designations appear at the bottom of each page, and pages included in each of the volumes are shown in parentheses at bottom of the cover.

(b) incentives necessary for the required exploratory effort; (c) adverse consequences of a rollback of rates to levels of the 1950's; and (d) effect of area rates allowed upon capital requirements and the exploratory effort needed to assure adequate supplies.

3. Whether the Commission erred in refusing to consider current evidence as to the decline in exploration and inadequacy of gas supply to meet foreseeable demand, and whether the Court of Appeals erred in affirming such refusal and denying a motion for leave to adduce such evidence before the Commission under Section 19(b) of the Natural Gas Act.

4. Whether in determining revenue requirements, the Commission erred in relying principally upon (a) "unit costs" based upon imprecise, unsupported, and erroneous allocation methods; (b) stale, atypical, and unrepresentative data to determine revenue requirements, conflicting with principles stated in *Baltimore and Ohio R. Co.* v. *Aberdeen & Rockfish R. Co.*, 393 U.S. 87 (1968); and (c) stale and unrepresentative data to determine level and sources of capital requirements, conflicting with the principles stated in *D. C. Transit System, Inc.* v. *Washington Metropolitan Area Transit Commission*, 350 F.2d 928 (D.C. Cir. 1965), and *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944).

5. Whether the Commission erred and misinterpreted *Permian* in failing to adopt a regulatory standard compatible with and appropriate for the characteristics of the natural gas producing industry; in using narrow, improper utility rate base cost of service methods; and in failing to employ regulatory methods and criteria suitable for the industry to be regulated and for the Commission's function of assuring adequate gas supplies at just and reasonable rates.*

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* This question is presented by Petitioner Continental Oil Company only.

STATUTES INVOLVED

Sections 4(a), 4(e), 5(a), 16, and 19(b) of the Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717-717w, are involved and are reproduced at Appendix F, pp. 1-8.

STATEMENT

This is an area rate case under Sections 4 and 5 of the Natural Gas Act. After hearings and by decision issued September 25, 1968, but based primarily upon 1960 data, the Federal Power Commission prescribed rates for sales of natural gas produced in onshore and offshore Southern Louisiana to be effective October 1, 1968 and also provided for the ordering of refunds. This area of approximately 54,000 square miles is the source of approximately one-third of the nation's interstate natural gas supply and serves the District of Columbia and 28 states in the eastern and central United States, in which approximately 70% of the nation's population resides. The effect of the Commission's decision was a rollback to prices considered "in line" as of 1956, and a reduction of area producers' revenues by more than $70 million per year (IV J. A. (I) 670d-671d, 683d).

However, by the time of issuance of all opinions below, there was increasing evidence of a national shortage of natural gas. The impact of that shortage began for many interstate pipelines in late 1969 and early 1970, and today is a recognized reality among all segments of the natural gas industry. The Court of Appeals concluded that imminence of this shortage and the related effect of the Commission-prescribed rates upon required exploratory effort and the industry's capital requirements in 1969, 1970, and the future, had not been properly considered by the Commission, particularly in light of new supply studies released by the Commission's Staff in late 1969 and other data that became available after the record closed in 1965 and after the issuance of the Commis-

sion's opinion on September 25, 1968. The Court of Appeals also found the Commission remiss in not following the opinion rendered by this Court in *Permian* on May 1, 1968, particularly in failing to give heed to this Court's numerous warnings that the Commission must consider the effects of prescribed area rates upon supply requirements, and admonitions that the Commission must improve its area-rate methodology, fact-finding, and decisional processes. With express "misgivings," the Court of Appeals affirmed the Commission, but on the assumption the Commission would reconsider its opinions and orders in the light of deficiencies enumerated by the court and the Commission's expressions of concern over supply. The court thus indicated that if current data warranted, the Commission was free to stay, rescind, and set aside any parts of its opinions and orders. Petitions for rehearing were filed by these and other parties raising questions as to Commission powers in light of "affirmance," and in response to inquiry from the court, the Commission filed a formal request for remand. Thereafter, the Court of Appeals did not change its "affirmance," but clarified and restated its intent that the Commission could and should reassess its opinions and orders; the Commission then entered an order further staying its orders, and today has before it a motion by these and other parties seeking reopening, rescission, and modification of the opinions.

Procedural History. The case was instituted on May 10, 1961 to fix rates for all jurisdictional sales of natural gas by producers in the Southern Louisiana area (III J. A. (I) 1d).[2] These petitioners are producers who were respondents before the Commission,[3] and the hundreds of

[2] This order defined the area as the portion of the State of Louisiana lying south of the 31° parallel and including all areas, both state and federal, in the Gulf of Mexico off the shore of Louisiana.

[3] As directed by the Commission, present petitioners participated and presented evidence cooperatively and were part of a group styled below as the Amerada, *et al.* Group.

parties included other producers, pipelines, distributors, and state commissions. Hearings commenced on December 10, 1963, and concluded November 5, 1965. The Commission's opinion and implementing orders were issued September 25, 1968, and timely applications for rehearing and motions for stay were filed under Section 19(a) of the Natural Gas Act (see IV J. A. (I) 764d). In these applications and in motions for limited reopening of the record, Continental, *et al.*, sought admission of then more current evidence reflecting *inter alia*, consideration of the *Permian* decision, the deteriorating national gas supply situation, rising costs, and other data relevant to rate design. On October 23, 1968, the Commission granted rehearing to consider all applications together (IV J. A. (I) 771d), but on March 20, 1969, issued its Opinion No. 546-A denying the applications, motions for stay, and motions for limited reopening, and modifying its original opinion in part only (IV J. A. (I) 892d). Simultaneously, the Commission instituted a new proceeding at Docket No. AR69-1 to consider new area rates, but only for gas-well gas sold under contracts dated on or subsequent to October 1, 1968 from the Offshore Federal Domain only (see IV J. A. (I) 896d).

Timely petitions for review were filed pursuant to Section 19(b) of the Act. The first such petition was filed in the Court of Appeals for the Fifth Circuit, and the Commission certified the record to that Court on March 26, 1969. Motions for partial stay and motions for leave to adduce additional evidence, particularly as to the supply situation, also were filed by producer petitioners. After a conference before the court, the Commission issued an order staying until October 13, 1969, the provisions of its orders requiring rate reductions, and this stay subsequently was continued by the court after argument on December 17, 1969.

The court's opinion was issued March 19, 1970; timely petitions for rehearing followed raising, *inter alia*, the

questions as to relationship between "affirmance" and Commission powers to reconsider and rescind its orders; the court thereupon requested Commission views, and in response, the Commission requested remand;[4] however, on June 16, 1970, the court denied the petitions, but reiterated that its "affirmance" was not intended to bar Commission reopening of any part of its order and retrospective as well as prospective changes of the orders by the Commission. The Commission entered its order continuing the stay as to rate reductions and refunds on July 2, 1970, effective upon dissolution of the court's stay; and on July 14, 1970, the court issued its judgment.

The Commission Opinions. Without significant change of methods criticized in *Permian*, the Commission prescribed area rates, but added a novel indefinite moratorium and method for future regulation. As noted, the end result is a rollback to price levels of the 1950's and insufficient revenues for current required exploration and development.

On the major issue of adequacy of supply, the Commission recognized a correlation between supply and price and responsiveness of needed exploration to price (Appendix D, pp. 67, 154-159). However, the Commission made no findings as to future demand or future gas supplies required to meet demand, particularly supply requirements from Southern Louisiana. Producers asserted these omissions as errors and cited mounting evidence of an impending gas shortage in seeking rehearing and limited reopening, urging the Commission to consider current data on supply, demand, and resultant capital requirements, and to make necessary findings (Appendix E, pp. 3-5). However, reopening was denied, leaving in effect the rates prescribed primarily on the basis of 1960 cost data and without consideration of current data on supply.

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[4] Chairman Nassikas and Commissioner O'Connor did not join in the request for remand.

In prescribing such rates, the Commission used costing methods requiring compositing of costs and expenses, determining an investment rate base, applying a rate of return to that base to arrive at the return allowance, adding these amounts, and ultimately dividing by volumes to arrive at average "unit costs." Using composited cost data, the Commission separately determined the cost per Mcf of "flowing gas" (Appendix D, pp. 85-107), and of "new gas-well gas" (Appendix D, pp. 29-84). The "flowing gas" cost was determined on the basis of composite historical averages for the 1960 test year, with some data on a national basis and some data on an area basis. The "new gas-well gas" cost was derived from data from numerous publications and questionnaires reflecting primarily 1960 data. With these data, the Commission (1) constructed a rate base for capitalized investment, applied to this base a 12% rate of return, added certain expense items, and derived a "unit cost" of 18.36¢ per Mcf for flowing or "first vintage" gas (Appendix D, p. 107); and (2) constructed a "current cost" model and derived a "unit cost" of 18.80¢ per Mcf for "second" and "third vintage" gas (Appendix D, p. 84). These two cost determinations then were used as the basis for prescribing the following maximum rates for different "vintages" of gas produced in onshore Southern Louisiana (Appendix D, p. 179):

a. *First Vintage* (Contracts dated prior to January 1, 1961)—18.5¢ per Mcf for all casinghead gas and gas-well gas and residue gas derived therefrom.[5]

b. *Second Vintage* (Contracts dated January 1, 1961 through September 30, 1968)—19.5¢ per Mcf for gas-well gas and residue gas derived therefrom, and 18.5¢ for all other types of gas:

[5] All rates are stated per Mcf at 15.025 psia unless otherwise indicated.

c. *Third Vintage* (Contracts dated on or after October 1, 1968)—20¢ per Mcf for gas-well gas and residue gas derived therefrom, and 18.5¢ for all other types of gas.

For gas produced offshore Southern Louisiana not subject to State taxes, area rates were fixed at 1.5¢ per Mcf lower for each vintage and type of gas.

All rates are subject to adjustment downward if Btu content of gas is less than 1,000 per cubic foot or upward if Btu content exceeds 1,050 (Appendix D, pp. 180-181). Third vintage rates also will be subject to downward adjustments for deviations from "pipeline quality" standards (Appendix D, pp. 179-180).

The Commission also issued a new regulation providing that area rates continue in effect until changed by Commission action, imposing an indefinite moratorium on rate increases for first and second vintage sales; a fixed moratorium on third vintage onshore sales until January 1, 1974; and an indefinite moratorium on offshore third vintage except for increases of 1.5¢ per Mcf collectable subject to refund only. The Commission also provided that producers could seek relief by filing petitions "to waive or lift the limitation on rate change filings" (Appendix D, p. 169), or by petitioning for rulemaking to amend the rates on an area basis (Appendix D, pp. 171-174). The orders accompanying the opinions also imposed requirements for filing rate schedule supplements reflecting rates prescribed, statements as to quality adjustments and resulting area rates, and reports of amounts subject to refund under Section 4(e) of the Act after application of the prescribed rates in consolidated rate suspension dockets. Actual payment of refunds of past collections remained subject to further order of the Commission, but in absence of stays, rate reductions would have been effective prospectively from October 1, 1968.

In a separate opinion on rehearing, Commissioner John A. Carver, Jr. dissented (Appendix E, pp. 72-112), em-

phasizing the central issue is whether prices fixed are sufficient to elicit adequate gas supplies, and ". . . a serious problem of gas supply has been identified, requiring action *in this case*" (Appendix E, p. 74). He noted that trends reflecting increasing demands and inadequate additions to reserves foretell deliverability problems which could lead to higher consumer costs; viewed "incentive" as negated by the rollback in rates, particularly because revenues from first and second vintage gas are the major source of capital funds for new investment; stated that substantial refunds and rate reductions amounted to retroactive expropriation of the "incentive" which had induced the initial commitment to interstate commerce; and concluded that the record supported fixing area rates at higher levels (Appendix E, pp. 110-112).

The Court of Appeals Opinions. The same central issue was recognized by the Court of Appeals, and the major theme of its opinions is that on the supply problem and related issues, the Commission had failed to follow this Court's admonitions in *Permian.* The court thus began with the statement that its "affirmance does not reflect full satisfaction with the performance that the Commission turned in . . ." (Appendix A, pp. 2-3), and ultimately concluded that in light of "new evidence of a possible impending gas supply shortage" (Appendix B, p. 1), the court intended to permit the Commission "to stay, modify or rescind any part of its order, notwithstanding our affirmance, if circumstances appearing since the issuance of the orders make a change advisable" (Appendix B, p. 2). Between these statements, the court found more than ample grounds to reverse the Commission on each of the questions now presented by Continental, *et al.* and to fashion a remand for corrective action by the Commission in accordance with such an opinion.

The court first traced evolution of producer rate regulation culminating in the *Permian* decision, which was

issued more than four months prior to the Commission opinion in the instant case. The court then summarized the Commission opinion, but noted that two days prior to oral argument before the court, the Commission had issued an order enlarging the scope of the new Docket No. AR69-1 proceeding to include the question of *prospective* adjustment of onshore and offshore Southern Louisiana area rates of all vintages (Appendix A, pp. 16-17). These and other indicia were taken to mean "that the Commission now recognizes the possibility of a serious supply deficiency and that it did not recognize this possibility in the decision we are reviewing" (Appendix A, p. 17, footnote omitted). In the court's view, however, this militated in favor of "affirmance rather than reversal," but subject to the court's expressions as to Commission powers and functions to modify its orders, discussed *infra*.

The court next considered substantive issues raised by these and other parties. It first rejected arguments that the cost determinations, rate of return allowance, and "noncost elements" were unsupported or "overly generous to producers" (Appendix A, pp. 18-30), and then turned to issues raised by these and other producer petitioners. On issues raised by the indefinite moratorium, the court found *Permian* not dispositive (Appendix A, pp. 31-32), but also found that the new regulation and an indefinite moratorium did not violate Constitutional requirements or the Administrative Procedure Act, and that Section 4 of the Natural Gas Act did not preclude an indefinite moratorium (Appendix A, pp. 32-36). On questions involving the Commission's rate of return, cost, and rate design determinations, the Court of Appeals was similarly "troubled" and critical. Thus, on the question of improper application of the "comparable earnings test" to determine rate of return, the court concluded producers "present persuasive evidence" that the test period used by the Commission was "unrepresentative" (Appendix A, pp. 39-40). On other questions as to costs

used, the court found *Permian* controlling and that Commission conclusions on issues as to use of stale, unrepresentative data were supported by statements "that costs as a whole" had been "remarkably steady (or were even declining slightly)" during the decade between 1960 and 1970; but, at the same time, the court stated its agreement with Commissioner Carver's dissenting view "that the Commission should not have relied upon cost calculations floating in a vacuum but should have reviewed its computations in light of supply, demand, and other market forces . . ." (Appendix A, pp. 45-46).

The "most serious issue" involving Commission findings and legal standards—termed "the supply problem" by the court—similarly gave rise to extensive, telling revelation of error (Appendix A, pp. 46-56). The Court of Appeals recognized that this Court held in *Permian* that "adequate findings" would be required in the future, but noted that the Commission had left gaps similar to the omissions criticized by this Court in *Permian*. Thus, the Court of Appeals found ". . . the Commission failed to approach supply and demand in either a semi-quantitative or qualitative way" (Appendix A, pp. 49-50), and listed defect after defect in "findings" on related questions of supply, demand, and actual availability of capital to the industry at rates prescribed (Appendix A, pp. 52-69). The court also noted existence of more current data available to the Commission, including the study by the Commission's Staff released in October, 1969, which indicates "perhaps a certainty, that the supply of gas is dangerously low" and "a serious shortage, in fact, may already be unavoidable" (Appendix A, p. 52). In sum, the court found that the assessment of the crucial facts as to supply, demand and impact of prescribed rates called for by *Permian* had not been made in this case.

Nevertheless, the court did not grant motions before it for leave to adduce current evidence before the Commission in accordance with procedures of Section 19(b), and

did not reverse and remand the case to the Commission. Instead, it expressed "serious misgivings about affirming the Commission" and did so only with affirmative statements that the Commission still may "set aside the present order pending further determination" (Appendix A, pp. 56-57); that "affirmance" is not a "judgment that the supply problem is not serious enough to require immediate modification of the order herein sustained" (Appendix A p. 59); that on "the crucial issue of sources for adequate financing, the Commission's findings, and for that matter the evidence, are almost nonexistent" (Appendix A, p. 63); that from the Commission's findings it is impossible to know current and future demand for Southern Louisiana gas, and supply must be considered in light of demand (Appendix A, pp. 65-68); that "the Commission must explain the relationship between the level of service, the demand for service, and the price it sets" (Appendix A, p. 68); that the "mandate" of the Court should not "be interpreted to interfere with Commission action that would change the rates" (Appendix A, p. 69); that, citing Section 16 of the Act and with emphasis supplied, the Commission had power to "rescind" its orders; and that dissolution of the court's stay would be without prejudice to Commission power "to stay its own order or to take any order or to take any other appropriate action affecting this case" (Appendix A, p. 70).

Petitions for rehearing by these and some of the other parties urged, *inter alia*, that express reversal and remand were required in light of the deficiencies in the Commission orders so found by the court, and also raised the question of whether an "affirmance" could leave the Commission with powers to stay, vacate, modify, or rescind its orders, as contemplated by the court. The court thereupon directed the Commission to respond to the petitions and to two specific questions concerning (1) Commission authority to stay, modify or rescind an order that has been "affirmed"; and (2) equitable powers of the court to "affirm" while preserving Commission powers "to stay, mod-

ify, or rescind" an order.[6] In response, the Commission (1) took the position that it would not "have authority to permit any *retroactive* increases or decreases in a rate order, unless authorized to do so by a court"; (2) stated that extent of the court's "equitable powers" had not been decided, and the court had "full statutory power to authorize or instruct the Commission" to "reconsider" the record or "reopen the record" for specific purposes "without necessarily reversing the Commission and vacating the order for a new hearing"; (3) noted the need for clarification of the court's intent to authorize "retrospective adjustments" in light of its "use of the words 'sustained in full' "; and (4) requested a "remand" so "that the Commission can discharge its regulatory responsibilities consistent with the Court's opinion." [7]

However, on June 16, 1970, the court entered an order denying the petitions for rehearing and an opinion stating that "affirmance of the Commission's orders is structured so as to allow the Commission great flexibility" (Appendix B, p. 1). The court stated that under Section 19(b) of the Natural Gas Act, the court had "broad remedial powers that inhere in a court of equity, and pursuant to our equitable powers we make it part of the remedy in this case that the authority of the Commission to reopen

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[6] The full text of the questions posed by the court is:

"(1) Whether the Federal Power Commission has authority to stay, modify or rescind an order once that order has been affirmed by this Court, if circumstances appearing since the entry of the order seem to make these actions advisable.

"(2) Whether this Court may, in the exercise of its equitable powers, affirm an order of the Commission while preserving the authority of the Federal Power Commission to stay, modify or rescind the order if the circumstances seem to make these actions advisable."

[7] "Response of Federal Power Commission to Petitions for Rehearing and Request for Remand," pp. 2-5 (Chairman Nassikas and Commissioner O'Connor did not concur in the request for remand).

any part of its orders, including those affecting revenues from gas already delivered, is left intact. The Commission can make retrospective as well as prospective adjustments in this case if it finds that it is in the public interest to do so" (Appendix B, p. 2). The court, nevertheless, emphasized that its "judgment is affirmance and not a remand," and that all issues as to reopening, modification of rates, and disposition of refunds were to be considered before the Commission (Appendix B, pp. 2-3).

REASONS FOR GRANTING THE WRIT

1. Importance of this case to all segments of the natural gas industry and all classes of consumers cannot be overstated. A shortage of natural gas already exists, as now recognized by the Commission and as feared by the Court of Appeals. That shortage is directly involved in this case because rates prescribed apply to an area that now provides up to one-third of the total national supply and serves more than one-half the consuming population of the United States. These rates were fixed primarily on the basis of 1960 cost data, without regard for the impending supply shortage, a decade of rising costs, erosive effects of inflation in the late 1960's, and compelling urgency for an increased national and area exploratory effort to attempt to find supply to meet increasing demand. As an immediate result, under the rates so fixed, amounts now exceeding $375 million, including interest, would be "refunded" to pipeline companies, and producers' rates and revenues would be rolled back to levels of the 1950's. The ultimate result would be an immediate, further decrease of capital available for needed exploration and a crippling blow to any effective industry effort, at present and for the foreseeable future, to avoid a serious national natural gas supply deficiency.

This result is not endorsed by the Court of Appeals, is not sought by the Commission in light of facts now available to it, and is not now urged by most who were

parties before the Commission and the Court of Appeals. The only valid question remaining is, in essence, how to remedy the situation so recognized by the court, Commission, and most of the parties, as promptly and as equitably as possible. To that end, the Court of Appeals attempted to fashion a remedy leaving the Commission free to take corrective steps present circumstances and known facts dictate, including rescission of the deficient orders reviewed below. However, the Court erred in failing to reverse and remand the case to the Commission. Several parties thus now question validity of any corrective steps by the Commission responsive to the Court of Appeals' opinions. Moreover, if the "remedy" assumed by the court below is *not* available as a matter of law, then the "affirmance" below rests upon serious misinterpretation of the Natural Gas Act as to Commission powers to act despite the affirmance. The corrective measures contemplated by the court thus can be foreclosed solely because of such misinterpretation and contrary to that court's intent; and the court erred in not entering a judgment of reversal and remand on the basis of its own opinions, of the request by the Commission for a remand, and of the objectives of corrective action stated by the agency and the court itself. *Sunray Mid-Continent Oil Co.* v. *Federal Power Commission*, 353 U.S. 944 (1957).

If the court below so erred in its holdings as to Commission powers to take corrective action and to rescind its orders in light of the court's opinions despite the "affirmance," then that court erred in entering and permitting conclusive finality for opinions and a judgment (1) conflicting with decisions of this Court as to required remand of cases under Section 19(b) once Commission error is apparent and corrective action is required; (2) conflicting with this Court's *Permian* opinion, particularly as to Commission responsibility for adequate supplies in applying the area rate method; (3) conflicting with *Permian* and other constructions of the

Act on major questions of capital requirements, cost determinations, rate design, and impact of area rate orders; and (4) incorrectly deciding issues as to relationships between administrative agencies and reviewing courts of major importance under the Natural Gas Act and of general significance and applicability in administrative law and under other federal statutes having review provisions similar to Section 19(b) of the Natural Gas Act.

2. Reversal and a remand by the Court of Appeals were fully warranted and proper dispositions under this Court's constructions of Section 19(b) of the Natural Gas Act. As reflected in *Federal Power Commission* v. *United Gas Pipe Line Co.*, 393 U.S. 71 (1968), the Court of Appeals' duty is to return cases by remand to the Commission "for further proceedings" when it concludes that the agency has erred by commission or omission, that reconsideration by the agency is appropriate, and that corrective action by the agency may be required.

Such established rules of agency-court relationships[8] are fully applicable under this statute. *Sunray Mid-Continent Oil Co.* v. *Federal Power Commission*, 353 U.S. 944 (1957). A remand order, therefore, was the logical, lawful, and required conclusion to the court's enumeration of a plethora of defects, inadequacies, gaps, and misinterpretations of *Permian*. The court thus stated what, heretofore, has been one of the predicates for judicial reversal, and, indeed, a requirement for remand of an agency order:

> ". . . A reviewing court contemplating the 'end result' test cannot in good conscience affirm the Commission unless it knows what the Commission is trying to do" (Appendix A, p. 68).

This statement alone compelled remand particularly in light of the court's conclusions that from the "Commis-

[8] See *Securities and Exchange Commission* v. *Chenery Corp.*, 318 U.S. 80 (1943); 332 U.S. 194 (1947); *Federal Power Commission* v. *Idaho Power Co.*, 344 U.S. 17 (1952).

sion's findings we cannot know" the future demand for Southern Louisiana gas, and without such findings the required levels of supply, of exploratory effort, and even of area rates cannot be known (Appendix A, pp. 66-67). The court also had found Commission findings "almost non-existent" on the "crucial issue of sources for adequate financing" (Appendix A, pp. 63-64), and these gaps alone should have precluded an "affirmance" that could, in any way, bar Commission correction of such errors.

Beyond this, the formal request for remand by the respondent agency clearly should have been honored if this Court's prior constructions of Section 19(b), rather than an "experiment doctrine", remain controlling. See *Sunray Mid-Continent Oil Co.* v. *Federal Power Commission*, *supra*. The Court of Appeals had stated, quite plainly, its own disapproval of the Commission's "performance," and that the court had "little inclination to join the Commission in presiding over" the possible "result" of a predicted "severe gas shortage" (Appendix A, p. 47, fn.87). Responsive to this criticism, the Commission requested remand and obviously desired fully to exercise its corrective powers in light of facts now available and without questions as to legality of its corrective action. The court nevertheless adhered to the remedy it had fashioned, which, in its first opinion, the court considered required by what it termed "the 'experiment' doctrine of *Permian*" (Appendix A, pp. 10, 60). Yet, Section 19(b) should not permit such a condemnation of the Commission to be coupled with denial of the agency's request for unquestioned power to correct the very errors on which the condemnation rests.

This case thus presents the question of whether *Permian*, or any other opinion of this Court, modified the relationship between administrative agencies and reviewing courts by creation of an "experiment doctrine" rendering reversal and remand inappropriate where the

agency opinion is defective. Where error exists and corrective action is required, the settled principles heretofore controlling would dictate reversal and remand for further proceedings consistent with the reviewing court's opinion. Therefore, the court erroneously may have rendered itself and the agency powerless to correct plain, recognized errors in this case. Under those circumstances, departure from settled principles and misinterpretation of *Permian* will have created such a result. All those adversely affected by the substantive errors revealed below—including the consuming public—can be left entrapped by provisions of orders the court should not have approved, and which the agency expressly desired remanded to it.

If the remedy fashioned below is not lawful, then the Court of Appeals' departure from this Court's earlier constructions of the review provisions of the Natural Gas Act cannot be allowed to stand. If the nature of the court's judgment can preclude such corrective Commission action as rescission or retrospective modification of its orders, this Court's review is essential to remove all doubts by reversal and remand as called for by the agency, by the Court of Appeals' own preliminary conclusions, and by prior constructions of Section 19(b) by this Court. Such orders of this Court also would provide the agency the latitude it sought by requesting remand and clarify the scope of statutory and equitable powers of a reviewing court under Section 19(b) of the Natural Gas Act and other statutes having the same or similar provisions for judicial review of agency orders,[9] particularly when a regulatory agency requests remand of its own opinions and orders.

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[9] See, *e.g.*, *Tacoma* v. *Taxpayers of Tacoma*, 357 U.S. 320 (1958); *International Union* v. *Eagle-Picher Mining & Smelting Co.*, 325 U.S. 335 (1945); *United States* v. *Seatrain Lines, Inc.*, 329 U.S. 424 (1951); *Civil Aeronautics Board* v. *Delta Air Lines*, 367 U.S. 316 (1961).

3. Related to the question of required remand are questions raised by the Commission's failure to follow the warnings of this Court in *Permian*, by Commission misinterpretation of *Permian*, and by any perpetuation of misreadings of *Permian* in future administration of the area rate method.

This Court thus called for responsible consideration of the interrelation of rates, capital, supply and demand as affirmative, express parts of the Commission's fact-finding and decisional processes. Gaps as to these most vital facts affecting interests of consumers on the one hand, and of investing producers on the other, were not contemplated by this Court. The Commission had more than four months to review this Court's *Permian* opinion before it entered its first opinion in this case, and more than ten months before it denied rehearing and motions to reopen. Yet, as found below, the Commission followed form without regard to substance. The Court of Appeals thus correctly was "disturbed" by the Commission's "excessive reliance" upon the mere "result" of *Permian* and correctly concluded that the Commission had not "read *Permian* carefully enough" (Appendix A, p. 60). However, the court's reluctance to label the Commission's errors as clearly reversible rested on that court's error in assuming that an "experiment doctrine" was intended to immunize decisions in subsequent area cases of such national importance as this case, even in the face of a critical supply situation, patent disregard of *Permian* by the Commission, and failure to make the most basic findings required in an area rate case.

On the "most serious" issue of supply, this Court's mandate to the Commission in *Permian* also was plain, requiring Commission "assessment of the consequences of its orders for the character and future development of the industry." [10] In our view, this Court did not au-

[10] *Permian Basin Area Rate Cases*, 390 U.S. 747, 792 (1968).

thorize an "experiment" even in a second major case where the adverse consequences are so apparent, as here, and the area is so vital to the total national supply. The court below thus erred in interpreting *Permian* as excusing all reversible errors. Consequences of repeated errors by the Commission include dissipation of capital funds that must be committed now to exploration if demand is to be met, and the continued inability of the industry to retain or even attract capital that cannot await round after round of "experiments" and possible proclamations of new area rates in another proceeding, four or five years hence. The record before the Court of Appeals, therefore, called for application of *Permian* as a precedent for ordering agency correction of reversible errors. However, this Court's instructions in *Permian* obviously must be repeated, and the misinterpretation of *Permian* in this case by the agency and the court below, including unfounded inhibitions of the court below to reverse plain errors, should be set aside.

4. Similar misreadings of *Permian*, *Hope*, and *Baltimore and Ohio R. Co.* v. *Aberdeen & Rockfish R. Co.*, 393 U.S. 87 (1968), have produced the questions involving (1) determination of costs, (2) determination of capital requirements, (3) use of atypical and unrepresentative data to determine revenue requirements, (4) application of these determinations in rate design, and (5) absence of required findings.

As noted below, ". . . . a reviewing court must look to both individual components and overall effect of rates set by the Commission," and the agency has "broad discretion." (Appendix A, p. 10). Yet, *Permian* also emphasized continued applicability of the *Bluefield*[11] and *Hope*[12] tests in determining a rate of return, of the

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[11] *Bluefield Water Works & Improvement Co.* v. *Public Service Commission*, 262 U.S. 679 (1923).

[12] *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944).

substantial evidence rule, and of the necessity for properly supported findings of fact on critical issues in rate cases under Sections 4 and 5 of the Act. On the questions enumerated by these petitioners (*supra*, pp. 2-3), it therefore is clear that the court's failure to reverse the Commission also resulted in large part from the error of assuming applicability of an immunizing "experiment doctrine" (see Appendix A, pp. 40-41).

For example, despite a general statement that the Commission adequately "explained" its cost findings, the court specifically noted important instances where critical cost and rate impact determinations are unsupported by findings. Such Commission failure to make findings on the components of its cost determinations and rates therefore remained grounds for reversal; and of particular significance was the failure of the Commission to consider consequences of its orders, and the court's recognition that the Commission's findings were deficient as to support for use of unexamined cost averages. The court indicates the Commission could eliminate these questions with findings as to whether use of such averages will prevent large segments of the industry from recouping investment and will lead to greater concentration in the industry (Appendix A, pp. 60-64), but the gaps are left unfilled in this case.

A related deficiency is the absence of Commission findings to support a conclusionary statement that capital from "outside sources" will be available for adequate financing, a statement the court notes is "a tenuous basis for our affirmance" (Appendix A, pp. 63-64). The court thus apparently did not appreciate that the missing findings on "averages" and the availability of "outside" capital are both directly related to a deficient gas supply by the Commission's own reasoning. The record thus shows that 53 of 81 producers will be unable to recover their costs at rates fixed, and as to these producers, the Commission held that it will provide no relief by way of

an increased price or by permitting abandonment.[13] Instead, the Commission held that such producers have the alternatives of achieving a fair return by *curtailing* their exploration and development program, or of assuming the risk that exploration and development will be profitable at the rates fixed in this case (see Appendix D, pp. 129-130). However, this very curtailment of exploration and development by a majority of producers necessarily will mean a lesser gas supply, and neither the Commission nor the court seemed to note that it is precisely this type of gap in the Commission's methodology, fact-finding, and rationale that *Permian* called upon the Commission to correct.

If, as the Court of Appeals assumed, the Commission now were free to correct all of these errors in findings and in determining costs, required return, and weight to be given these costs in rate design, the practical consequences and effect of erroneous precedent could disappear. However, if these determinations in this case stand, each stands as a reversible error predicated on misreading of *Permian* and upon unlawful relaxation of requirements for express, clear, specific agency findings resting on substantial evidence and for a lawful "end result" in a rate case. Each such question therefore will warrant review by this Court to correct misapplication of *Permian*, to preclude repetition of the same errors in Commission area rate decisions, and to minimize the practical consequences of inadequate rates and supply deficiencies caused by such defects in the Commission's process of fixing area rates.

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[13] The Commission's categorical statement that it would not permit abandonment is to be compared with the Court's holding that the lawfulness of using cost averages would be "a different question" if persons regulated were prevented from going out of business when revenues fell below costs (Appendix A, p. 42, fn.76). The Court thus further erred in determining the issue of lawfulness on an erroneous view of the Commission's own holdings.

5.* The Commission first began the area rate proceeding experiment in 1960. This Court endorsed this experimental approach by the Commission in *Wisconsin v. Federal Power Commission*, 373 U.S. 294 (1963). In *Permian*, this Court approved with reservations, recognizing the experimental nature of the area rate concept, the Commission's first endeavors in the *Permian* case. However, this Court in *Permian* admonished the Commission to reconsider its regulatory methods and expressed considerable doubt of the validity of the results reached in the first area rate case. Nevertheless, the Commission has, without substantial or appropriate modification, followed the narrow utility cost concepts applied in the Commission's Opinion No. 468 which culminated in the *Permian* case before this Court. This *Permian* cost concept of regulation thus has permeated all subsequent area rate proceedings before the Commission and has become the "institutional characteristic" of the examiners' decisions in the *Southern Louisiana*, *Texas Gulf Coast*, *Hugoton-Anadarko*, and *Other Southwest* area rate proceedings before the Commission, wherein the examiners have, without question or reconsideration, followed religiously the costing methodology employed by the Commission in *Permian* Opinion No. 468. As evidenced in this case, the Commission itself so continued to follow the narrow and ill-suited regulatory methods which it roughly fashioned in the *Permian* case.

While national supplies dwindled, the Commission thus continued to engage in futile exercises in utility rate base cost of service regulatory methods even though exploratory endeavors continued to decline and the gas supply has fallen critically in relation to demand. The conclusion thus is apparent now that the Commission's ill-founded and unsound regulatory concepts have hastened, if not caused, the present critical gas supply shortage. The Commission nevertheless continued to indulge

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* This section pertains to Question Presented No. 5 by Petitioner Continental Oil Company only.

in a fantasy that producer prices can be determined on the same basis that rates are established for traditional public utilities. However, in view of the disastrous results of sixteen years of Commission regulation which has so failed to make the essential departure from utility cost of service concepts, this Court should re-examine its sanction of Commission efforts in the *Permian* case and direct the Commission to employ regulatory methods compatible with the economic characteristics of the gas producing industry and to discontinue futile, dangerous efforts to regulate natural gas producers by public utility methodology.

This Court should no longer defer so instructing the Commission, through remand and direction in this case, as to the appropriate course in fashioning and employing regulatory methods for determining producer gas rates. This Court can so determine, as matters of law and fact, on the record in the present case, that the cost-of-service methods devised by the Commission in *Permian* and pursued in the instant Southern Louisiana area rate case cannot afford a valid or proper basis for producer rate regulation. In sum, the court below erred in misreading *Permian* as permitting the "experiment" in this case, and this Court's review is essential if this error is to be corrected.

6. The opinions of the Court of Appeals began and ended with expressions of concern over decline in supply and indicia of inability of the industry to meet even the present demand for natural gas. A statement of reasons this case warrants review by this Court necessarily must begin and end with similar reference to what is now a "serious supply deficiency" of national concern (see Appendix A, pp. 3, 68). The Court of Appeals did not err in calling upon the Commission to reconsider *all* parts of the opinions and orders on review in this case, and the Commission did not err in requesting an express remand and removal of any possible doubt as to its powers to take any required responsive action in-

cluding rescission of the defective orders.[14] Such Commission action could have been the most expeditious means of removing the legal errors, erroneous precedent, defective rates, and adverse supply consequences created by the opinions and orders reviewed below. However, questions raised as to the judgment below now warrant review to insure that the court below left no bars to corrective Commission action. Otherwise, solely because of technical wording, the substantive remedies, responsive action, and efforts to ameliorate the supply deficiency can be cut off, despite the clear intent of the court below and the Commission's request for remand. Such a disposition of this case would be detrimental to all segments of the natural gas industry and to the consuming public. Therefore, the questions presented by this petition should be considered by the Court.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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[14] By their petitions for rehearing, these petitioners likewise sought formal reversal and an express remand order for similar reasons.